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21 May 2012

Mr E J Hall
Chief Executive
Queensland Competition Authority
GPO Box 2257
Brisbane QLD 4001

Dear Mr Hall

The SEQ Water Grid Manager (the Water Grid Manager) makes the following submissions on the draft report on SEQ Grid Service Charges 2012–13.

Draft capital charges

The Water Grid Manager notes that the Authority has reviewed a sample of completed and proposed capital projects and has found that a high proportion of that expenditure was not considered to be prudent and efficient, or required further justification. For example, for projects to be commissioned in 2012–13:

- Seqwater proposed \$57.7 million of capital expenditure.
- The Authority and SKM reviewed \$24.0 million of that expenditure (about 42%).
- The Authority's draft recommendation is that only \$18.0 million of that sample is prudent and efficient (about 75%).
- The balance of the proposed capital expenditure is assumed to be prudent and efficient.

For projects that proposed to be commissioned beyond 2012–13:

- Seqwater proposed \$300.5 million of capital expenditure.
- The Authority and SKM reviewed \$152.6 million of that expenditure (about 51%).
- The Authority's draft recommendation is that only \$55.6 million of that sample is prudent and efficient (about 36%). It recommends that 13 of 17 projects are either not prudent or require further justification.

- The balance of the proposed capital expenditure is assumed to be prudent and efficient.

Similarly, the draft report states that both Seqwater and LinkWater have submitted insufficient information to demonstrate that all of the expenditure made in 2011–12 was prudent and efficient.

These findings may reflect systemic issues, which apply equally to the proposed capital expenditure that has not been reviewed by the Authority. We therefore recommend that the Authority not endorse proposed capital expenditure to be commissioned, or commenced, in 2012-13 unless and until it has been specifically assessed for prudence and efficiency.

In undertaking that assessment, we continue to be concerned that the project specifications for new water treatment plants are more stringent than what is required under our Grid Contracts. These concerns are outlined in our previous submissions, such as in relation to the proposed Kilcoy water treatment plant. We have similar concerns in relation to the level of reliability required, especially given the surplus capacity currently available within the system. We are available to assist the Authority in this regard.

We also recommend that the Authority specifically consider the timeframe within which any prudent expenditure is undertaken. We believe that there may be opportunity to stage some of these works, taking into account surplus capacity within the system and the small number of recent incidents. The staged delivery of prudent capital expenditure would have multiple benefits, in addition to reducing the proposed capital charge in 2012–13. Those benefits include providing reduced need for project delivery staff and time for long-term demand trends to be better understood, reducing the risk of oversized infrastructure. Given Government policy to merge the bulk water entities, it would also maximise the extent to which that entity may determine the capital program that it is responsible for delivering.

Finally, the Water Grid Manager endorses the position of the Authority that, unless there is other compelling information, the absence of a relevant planning study and options analysis will normally exclude the proposal from inclusion in Grid Service Charges in the relevant year. We consider that such studies should be required to demonstrate that proposed expenditure has been optimised to the project specifications.

In relation to specific projects, the Water Grid Manager generally endorses the Authority's analysis. However, we remain of the view that the proposed improvements to the Jimna and Boonah-Kalbar water treatment plants are not required at this time. Seqwater is currently consulting with us regarding the justification for, and scope of, proposed upgrades to the Boonah-Kalbar Water Treatment Plant.

Draft operating costs

The Water Grid Manager recommends that the Authority consider setting an efficiency target for Grid Service Providers, such as by capping operating costs at or below actual 2011–12 levels (without allowance for inflation).

The Water Grid Manager believes that operating costs could be materially reduced without increased service delivery risks. We do so based on our unique involvement in the strategic operation of the supply chain. That involvement includes system operations, emergency management, communications and contractual and financial arrangements.

Specifically, we consider that significant savings could be achieved based on the following:

- Across the supply chain as a whole, water supply operating costs appear to be higher in South East Queensland than in other capital cities. This comparison is in part reflected in the benchmarking undertaken by SKM, which is summarised in the draft report. However, it is more evident if costs are compared across the water supply chain as a whole, excluding wastewater and stormwater related costs.
- The draft report identifies several areas of duplication between existing entities. This duplication is likely to be reduced under the Government policy to review water supply arrangements.
- The number of staff involved in asset planning and delivery functions could be significantly reduced from that previously proposed, in line with the revised capital program outlined above.
- Residual water supply risks can be managed through the combination of maturing processes and systems and system capacity and interconnectivity. Those processes and systems include the emergency management framework, the effectiveness of which was demonstrated as part of the response to the January 2011 flood event.
- Grid Service Providers have consistently and substantially underspent operating cost budgets.

Annual Operations Plan

A updated version of the Annual Operations Plan will be submitted to the Queensland Water Commission on 28 May 2012 for approval. We will provide a copy of the proposed Plan at that time.

The proposed Plan reflects our previous submission to the Queensland Competition Authority. Among other matters, it states that no supply will be required from the Caboolture, Woodford and South Maclean water treatment plants in 2012–13. It also states that no supply will be required from the Banksia Beach water treatment plants in normal operations, but that they are required to remain available to provide supply in response to emergencies or customer requests.

We are currently consulting with relevant entities regarding the transition to the preferred mode of operation. That transition may involve the treatment of some water in 2012–13. For plants that are required to remain available, including Banksia Beach, a minimal amount of water may need to be treated to ensure that the plants are capable of providing supply if and when so instructed.

The Water Grid Manager remains available to assist the Authority in any way possible. Please do not hesitate to contact Mr Barry Dennien, Chief Executive Officer, on telephone 3033 0785 or via email at barry.dennien@seqwgm.com.au.

Yours sincerely



Gary Humphrys
Chair